INTEREXCHANGE CALLS FACILITATED BY VNXX DIALING ARRANGEMENTS ARE NOT ELIGIBLE FOR RECIPROCAL COMPENSATION OR ISP-BOUND COMPENSATION

- The *ISP Remand Order* Did Not Provide for ISP-bound Compensation for Traffic Between Dial Up Customers and ISPs In Different Exchanges

    - The history of the Commission's reciprocal compensation rules and the dispute over ISP-bound traffic confirm that the only ISP-bound calls at issue—and thus the only traffic subject to the compensation mechanism in the *ISP Remand Order*—were those in which the dial-up customers and ISPs were in the same exchange.

        - The Commission's original reciprocal compensation rules allowed reciprocal compensation payments only for "local telecommunications traffic." 47 C.F.R. § 703(a)(1996). *See also Local Competition Order* ¶ 1034 ("We conclude that section 251(b)(5) reciprocal compensation obligations should apply only to traffic that originates and terminates within a local area.")

        - Accordingly, the issue presented to the Commission with respect to ISP traffic was whether such traffic was "local" and thus subject to reciprocal compensation payments. *See ISP Declaratory Ruling* ¶ 1 ("Generally, competitive LECs contend that this is local traffic subject to the reciprocal compensation provisions of section 251(b)(5) of the Communications Act of 1934.")

            - CLECs claimed that ISP-bound calls terminated at the ISP. *See ISP Declaratory Ruling* ¶ 7 ("If these calls terminate at the ISP's local server (where another (packet-switched) 'call' begins), as many CLECs contend, then they are intrastate calls, and LECs serving ISPs are entitled to reciprocal compensation for the 'transport and termination' of this traffic.")

            - CLECs also claimed that ISP-bound calls were no different than local calls to other businesses. *See, e.g., Bell Atlantic v. FCC*, 206 F.3d 1, 7 (D.C. Cir. 2000)("In this regard, an ISP appears, as MCI WorldCom argued, no different from many businesses, such as 'pizza delivery firms, travel reservation agencies, credit card verification firms, or taxicab companies,' which use a variety of communications services to provide their goods or services to their customers.")

- *A fortiori*, the only calls that could have been in question—the only calls that CLECs possibly could have claimed were subject to reciprocal compensation under the Commission's rules then in effect—were calls in which the originating caller and the ISP's server were in the same local exchange.

    - The Commission was clear that its rules were designed to "resolve the problems associated with the *current* intercarrier compensation regime for ISP-bound traffic." *ISP Remand Order* ¶ 77 (emphasis added).

- Thus, the scope of the Commission's ISP-bound compensation mechanism in the *ISP Remand Order* is necessarily limited to calls between dial up customers and ISPs located in the same exchanges.

- The Commission's orders and the D.C. Circuit's decisions confirm that the Commission's ISP-bound compensation mechanism is limited to calls between dial-up customers and ISPs in the same exchange.

    - *ISP Declaratory Ruling*

        - ¶ 4: "Under one typical arrangement, an ISP customer dials a seven-digit number to reach the ISP server *in the same local calling area*." (Emphasis added.)

    - *ISP Remand Order*

        - ¶ 10: "As we noted in the *Declaratory Ruling*, an ISP's end-user customers typically access the internet through an ISP server located *in the same local calling area*." (Emphasis added.)

        - ¶ 13: "As a result of this determination [from the *Local Competition Order* that reciprocal compensation is due only on "local" traffic], the question arose whether reciprocal compensation obligations apply to the delivery of calls from one LEC's end-user customer to an ISP *in the same local calling area* that is served by a competing LEC." (Emphasis added.)

    - D.C. Circuit *Bell Atlantic* decision

        - "In the ruling under review, [the Commission] considered whether calls to internet service providers ("ISPs") *within*

the caller's local calling area are themselves local." *Bell Atlantic v. FCC*, 206 F.3d at 2. (Emphasis added.)

- D.C. Circuit *WorldCom* Decision

  - "In the order before us, the Federal Communications Commission held that under 251(g) of the Act it was authorized to "carve out" from 251(b)(5) calls made to internet service providers ("ISPs") located *within the caller's local calling area*." *WorldCom v. FCC*, 288 F.3d 429, 430 (D.C. Cir. 2002). (Emphasis added.)

- It would be arbitrary and capricious for the Commission to now determine that compensation for ISP-bound traffic between dial-up customers and ISPs in different exchanges is determined by the identity of the party being called rather than the locations of the calling and called parties.

  - If the Commission meant to expand intercarrier payment opportunities for ISP-bound traffic in which the dial-up customer and the ISP are located in different exchanges, *i.e.*, to alter the access rules for interexchange traffic as applied specifically to traffic bound for ISPs (or more generally for VNXX-facilitated interexchange traffic), it never said so, and never propounded any rationale for doing so in its orders.

  - Although the policy goal underlying the *ISP Remand Order* was to limit the arbitrage opportunities afforded by reciprocal compensation payments for ISP-bound traffic, the Commission's "mirroring" rule makes clear that the Commission did not effectuate that goal by proclaiming the identity of the called party, rather than the locations of the calling and called party, as the determining factor for determining compensation due for ISP-bound traffic. *See ISP Remand Order* ¶ 90 ("We therefore are unwilling to take any action that results in the establishment of separate intercarrier compensation rates, terms, and conditions for local voice and ISP-bound traffic. To the extent that per minute reciprocal compensation rate levels and rate structure produce inefficient results, we conclude that the problems lie with this recovery mechanism in general and are not limited to any particular type of traffic.")

- There Is No Legally Defensible Reason for the Commission To Declare VNXX-Facilitated Interexchange Calls Eligible for Either Reciprocal Compensation Or ISP-Bound Compensation

- There is no legally defensible rationale for imposing different intercarrier compensation obligations on VNXX-facilitated interexchange traffic and "traditional" interexchange

- Applying the ISP-bound compensation mechanism to calls between dial-up customers and ISP servers in different exchanges would be plainly and fundamentally antithetical to the purpose underlying the *ISP Remand Order*

    - The purpose of the *ISP Remand Order* was to "limit the regulatory arbitrage opportunity presented by ISP-bound traffic." ¶ 2. *See also* ¶ 7 (Commission's interim recovery scheme intended to "eliminate arbitrage opportunities presented by the existing recovery mechanism for ISP-bound traffic"); ¶ 71 ("ISPs do not receive accurate price signals from carriers that compete, not on the basis of the quality and efficiency of the services they provide, but on the basis of their ability to shift costs to other carriers.")

    - The intent was thus not to create a separate payment mechanism for all ISP-bound traffic. It was to *limit* the amount of such payments, and eventually eliminate them entirely.

    - Any action now—nearly four years after the Commission established its transition to bill and keep for ISP-bound traffic—that further entrenches and even perpetuates any such compensation would be contrary to the purpose and goals of the *ISP Remand Order*.

- The Commission already has in place a subsidy for ISPs (the ESP exemption), and there is no public policy justification to add to such subsidies by perpetuating ISP-bound compensation payments for the CLECs who serve them.

    - It is particularly inappropriate to perpetuate such subsidies for dial-up Internet access given the goal of the President, Congress, and the Commission to promote broadband deployment.

- Moreover, allowing such payments would favor CLECs with a business plan limited to serving ISPs over all other LECs (including CLECs) who serve residential customers, when the Commission specifically warned CLECs who served primary ISPs to "formulate business plans that reflect decreased reliance on revenues from intercarrier compensation" given the "strong possibility that the *NPRM* may result in the adoption of a full bill and keep regime for ISP-bound traffic." *ISP Remand Order* ¶ 83.

- Allowing ISP-bound compensation for traffic between dial up customers in one exchange and ISP servers in other exchanges will lead to absurd and legally indefensible results

    - There is no logically justifiable means of containing such result to arrangements based on the use of VNXX dialing arrangements. The logic is premised solely on the identity of the called party as an ISP (*See, e.g.*, PacWest Ex Parte (01-19-05) at 2 n 11 ("…the *ISP Remand Order* established the identity of the called party, not its location, as the principal factor for determining whether the federal intercarrier compensation regime for ISP-bound traffic is applicable."); *Id.* at 3 ("The *ISP Remand Order* makes clear that the new federal regime applies to *all* ISP-bound traffic."); CompTel Ex Parte (01-27-05) at 1 ("the FCC's interim rate plan, which makes no distinction between 'local' and 'non-local' traffic, applies to all ISP-bound traffic.") and thus applies to all calls to dial-up ISPs.

    - Under this theory, 1+ interexchange calls and even 800 calls— even if they originate in one state and connect with an ISP server in a distant state— would no longer be subject to access charges, as long as they were ISP-bound calls. *See* PacWest Ex Parte (01-19-05) at 7 n. 30 ("Verizon and BellSouth claim that the Commission has already determined that interLATA FX is a toll service subject to access charges, but they do not cite any case to support their claim.")